REPLACEMENT IN THE MARKET.

The doctrine of avoidable consequences is not generally considered as founded upon any *duty* resting on the plaintiff to reduce damages as far as possible; it springs from the idea that by consequences of a wrong which the plaintiff, acting as rational and prudent men normally do, can avoid, he is not legally damaged. In a number of cases the steps taken by the plaintiff to avoid in his own interest the consequences of the wrong, take the form of *replacement in the market.* The most common instances are cases in which the vendor has broken a contract for the delivery of goods sold, cases involving the purchase and sale of securities, or contracts to carry stocks; cases of conversion and replevin, and generally all cases involving the non-delivery or conversion of property by the defendant.[1] The simplest of all instances is the ordinary case of a sale in the market where the vendee, failing to receive the thing bought, immediately replaces himself by the purchase of other goods of the same sort at the market price.

There can be no duty of replacement in ordinary mercantile contracts nor in any of the other cases above referred to. That is to say, the plaintiff, by the mere fact of a breach of a contract or tort of this sort by the defendant, cannot be placed under a duty to make a contract with a third person to supply himself with that of which he has been deprived. The difference between such cases and those of the ordinary breach of contract of service, where the defendant can always show that the plaintiff is in default if he has not *employed his time* so as to reduce damages, is that in these cases the suit is based entirely on the loss of the value of time, and the failure of the plaintiff to employ his time so as to reduce damages is obviously a voluntary failure to act as a prudent and rational man normally would in his own interest; and his interest coincides to this extent with that of the defendant, so that the analogy here between his natural course of action in his own interest, and what would be his course of action if he were acting under a duty toward the defendant, is very nearly complete. But in the case of breach of ordinary mercantile contracts and of torts involving the conversion or non-delivery of property, it very rarely happens that the idea of duty to the defendant can properly be invoked, and we think it may be said broadly,

[1]See Sedgwick on Damages, §§ 507-525, 735, 745-749, 855; Sedgwick, Elements of Damages, pp. 262, 263, 310.

notwithstanding many dicta in the cases to the contrary, that in these cases, the plaintiff is *under no duty* to replace himself in the market. Our object here is chiefly to show the causes of the confusion on the subject of replacement which abound in the decisions, and how that confusion may perhaps be cleared up.

A wrong sounding either in tort or contract, or both, having been done, there are two possible cases of replacement. The person injured may replace himself, or he may be replaced by the wrongdoer. In the latter case, the question raised is that of the allowance of *benefits,* in which the rules of avoidable consequences have no place. The case which concerns us here is that of replacement by the party injured. The origin of the confusion on the subject is to be found in the fact that in many of the most familiar transactions of business, and wrongs connected with them, in which *market value* at the time of the wrong done furnishes the normal measure of damages, this measure is, owing to this very fact, the same as the cost of replacement. Whenever the plaintiff is deprived of property, or rights, through negligence, trespass, conversion or non-delivery, the normal measure of damages is the value of the property or rights at the time of the breach of contract or tort. Whenever there is a market, the value is determined by it. But since the plaintiff, if he replaces himself, must do so by a purchase at the market value, the cost of replacement, and the market value, are one and the same.[2] Hence, by a natural confusion, it is easy to fall into the error of laying it down that the cost of replacement is the measure of damages; and from this it is but a step to imagine that a *duty rests upon the plaintiff to fix the measure of damages* by replacing himself in the market. The substitution of the conception of a duty to replace for that of a resort to the cost of replacement as a measure, has led, and is still leading, to the formulation of anomalous rules quite at variance with the underlying principles on which the law of compensatory relief rests—indemnity and certainty.[3]

[2]A common case is that of directions to an agent to buy or sell, changed by error of an intermediate agent in transmission, *e. g.,* by a telegraph company. Rittenhouse *v.* Ind. L. of Telegraph (N. Y. 1865) 1 Daly 474; (1870) 44 N. Y. 263; Tyler *v.* W. U. Tel. Co. (1871) 60 Ill. 421; De Rutte *v.* N. Y. A. & B. T. Co. (N. Y. 1866) 1 Daly 547.

[3]Suydam *v.* Jenkins (N. Y. 1850) 3 Sand. 614. The opinion of Duer, J., in this replevin case is to-day the best guide that we know of through the whole labyrinth of cases which, since the abolition of the old forms of action, have endeavored to find some new rule of damages in actions for conversion or non-delivery of personal property beyond that of the value lost, increased by consequential damages, and limited by the rule of avoidable consequences.

Perhaps the best reason for the use of replacement as a test is that wherever property or property rights are taken, destroyed or injured, the person to whom they belong is entitled immediately to an amount of money representing the value *for all lawful purposes;* one of these being enjoyment and use, and another, sale, he is entitled at least either to the opportunity of replacement, or its value; *i. e.,* the sum for which he could have either bought or sold in the market, in other words, the market value.[4]

Were replacement a duty there would be some corresponding right in the wrongdoer. The cases, however, are totally silent on the subject of such a right. In the case of breach of contracts to carry stocks on margin, we hear of the plaintiff's right to call upon the defendant to replace him, and the plaintiff's duty to replace himself. The former is usually merely the right of the pledgor of stocks against money borrowed to call upon the pledgee if the latter has sold them without notice, or converted them, to restore the pledgor to the original position of which the defendant's wrong has deprived him; the latter is not a duty at all, but is suggestive of one by analogy in its involving an act on the part of the plaintiff which results in benefiting the defendant by arresting the consequences of his act, though actually a voluntary act dictated by self-interest.[5]

The cases which have caused most difficulty and have been productive of most confusion are those involving speculative contracts for carrying stocks. A broker, with whom a margin, *i. e.,* a certain percentage of the par value of the stocks purchased is deposited, buys for the account of a customer a number of shares to be held subject to the latter's orders. The broker may call for more margin if the stock declines in value; in other words, the percentage of margin must be "kept good." Such a contract is usually regarded as involving a purchase of stock, the customer becoming the owner and the broker the pledgee with a power to sell if the margin is not kept good, but not without notice. But it is also something else—a continuing speculative venture with borrowed money secured by the collateral of the stock and terminable at will, according to its terms, by either party, but on notice only. If the broker converts the stock to his own use by sale, the customer on discovery of the fact may disaffirm the sale and call upon the broker to replace, or may replace himself. The

[4]Sedgwick, Elements of Damages, p. 129; Smith *v.* Griffith (N. Y. 1842) 3 Hill, 333, 337.

[5]The metaphor is so close that in all cases, to exclude the use of the word "duty" without cumbrous circumlocution, is not easy.

measure of damages for conversion by the broker (which will be discussed hereafter in detail) has been held at different times and in different jurisdictions to be, first, the highest value of the stock in the market down to the time of trial; second, the highest intermediate value within a reasonable time after notice of the fact of conversion, and third, in accordance with the usual rule in conversion, the value at the time of the conversion.

The first measure of damages is founded upon the idea that as the customer *might* have replaced himself in the market if he had had notice, and so might have got the benefit of any subsequent rise in price, he is entitled to whatever profit he might have realized down to the trial. But this theory of the damages has been generally abandoned and it is wholly speculative and uncertain. He might *not* have replaced himself at all, and there is no possible way of proving that he would have replaced himself, if at all, at the right moment. There is here no suggestion that replacement is a duty.

The second measure of damages was established in New York by the leading case of *Baker* v. *Drake.*[6] Before the case of *Baker* v. *Drake,* the rule in New York, as established by *Markham* v. *Jaudon,*[7] had been that of the *highest intermediate value,* and although *Baker* v. *Drake* has been often misquoted or misapplied, the authority of the decision and of the opinion of the court, delivered by Rapallo, *J.*, has never been shaken. This fact justifies a close examination of the case at this early stage of our inquiry.

The facts involved were those of an ordinary contract to carry stocks on margin, as described above. The court in laying down the rule of damages did not treat the matter as one involving any distinction between tort and contract, but decided the case as one in which the rule was equally applicable whether the action was regarded as brought for a breach of a special continuing contract to carry stocks on a margin, or as an action of trover in which the plaintiff as owner sued for the conversion of goods pledged. In either case there is room for consequential damages—in the case of a contract, the loss of "probable profits,"[8] in that of conversion, the actual enhancement of the value of the stock converted down to a reasonable time within which the plaintiff might, had he not been kept in ignorance of the sale, have fixed

[6](1873) 53 N. Y. 211, 13 Am. Rep. 507. *Cf.* Gruman *v.* Smith (1880) 81 N. Y. 25; Colt *v.* Owens (1882) 90 N. Y. 368.

[7](1869) 41 N. Y. 235.

[8](1873) 53 N. Y. 216.

the amount of the loss. The decision and rule seem to involve the following conclusion: whenever the action is held to be conversion, it is because the contract of purchase is held to vest the *title* in the customer; the broker becomes the selling agent for the customer, and consequently commits a double wrong in selling without notice; he not only converts the property, but converts it without notice to the owner, his principal, and as between principal and agent this is an independent wrong,[9] which consists in the breach of a contract not to sell without notice; and unless the plaintiff is compensated for this wrong, which necessarily lasts until the expiration of a reasonable time after actual notice to replace himself, he loses part of the value of his right of redress. This seems to justify the New York rule in the case of an ordinary broker's contract to carry stocks, and to show the point of divergence which separates this class of cases from those of simple conversion, and also from sales, etc., etc. It also shows how mistaken is the idea that the rule of damages is dependent upon the notion that the plaintiff is under a *duty to replace.* The damages recoverable were said to be merely such as *"a proper degree of prudence* on the part of the complainant would not have averted." In other words, consequences not avoidable by the complainant acting with ordinary prudence, *i. e.,* from self-interest.

The third rule of damages given above is merely the ordinary rule in all cases of conversion or non-delivery of personal property—the value of the property at the time and place of conversion, or failure to deliver. This in itself does not invoke any duty to replace at all, and is merely the rule in the old action of trover or trespass *d. b. a.* But it is not a hard and fast rule, as will be seen when we come to deal with the subjects of conversion, trespass, sales, etc.[10]

In this class of cases *consequential damages* are always admitted so far as provable, and as limited by the rule of avoidable consequences. Now the rule of the value at the time and place of conversion, modified in proper cases by the allowance of *consequential damages,* is merely Rapallo, *J.'s,* rule of the actual enhancement down to the reasonable time within which plaintiff *might,* had he not been kept in ignorance of the sale, have fixed the amount of the loss (avoidable consequences); or of "probable profits" if the action be regarded as contractual.

[9]Brown *v.* M'Gran (1840) 14 Pet. 479, 496, 10 L. Ed. 550; Sedgwick, Elements of Damages, p. 293.

[10]Wallingford *v.* Kaiser (1908) 191 N. Y. 393, 84 N. E. 295.

A comparison of the three rules given above, therefore, shows that the only fixed measure is the value at the time of conversion or non-delivery; that the circumstances of the case may let in "reasonable profits"; an enhancement of damages (consequential) growing out of the loss of a reasonable opportunity for replacement due to deprivation of notice, or growing out of such other circumstances as may appear. Therefore, finally, the only general rule of damages in all such stock contracts is the value of the property or property rights lost (direct), enhanced by consequential damages within the limits fixed by the rule of avoidable consequences.

There is no essential difference on principle in the rule of damages between cases in which stocks are carried on margin and those in which they are bought for investment.[11] The measure is the value of what is lost. The facts are always the same, first, a conversion or failure to deliver with or without notice; second, a reasonable interval of time after notice, during which the natural, normal impulse of one who is the owner of property for any purpose may be to replace. At what price within this period would he naturally replace himself? This, in a proper case, is the value of *what he has lost* and therefore measures it. If the contract to carry is a continuing contract of the sort described above, he may demand that the defendant shall replace *him*, and it is not until this demand is refused that he is obliged to decide whether he will replace himself. Consequently, there may be a considerable interval of time before the moment arrives at which, as a reasonably prudent man, he will be called upon to determine whether to replace himself or not. That reasonable moment is determined by the jury and the value of what has been lost is fixed.

In cases of conversion of stocks without notice the interval is usually considerable; in those of failure to deliver goods under mercantile contracts, very brief; indeed the failure to deliver is usually known on the spot. In the former cases, any damages allowed over and above the difference in value at the instant of conversion, may be considered a species of consequential damages caused by the interval of time between the actual conversion and the reasonable time after discovery, for the privilege of replacement to be exercised. In margin contracts, the measure of damages is the difference between the price obtained by the broker and the highest price reached between the time the customer

[11] Wright *v.* Bank of The Metropolis (1888) 110 N. Y. 237, 18 N. E. 79.

learned of it, and a reasonable time thereafter.[12] If no time is required for decision, there is no interval.[13]

Unfortunately some courts, especially those of New York, have mistaken the rule properly *applied* in *Baker* v. *Drake* for a general rule of damages applicable to all stock-carrying contracts, and have substituted for the right of the plaintiff to have an opportunity to replace himself in case of deprivation of notice, a *duty* of replacement on his part. This duty is spoken of in *Wright* v. *Bank of the Metropolis* as "the duty of the plaintiff to make the damages as light as he reasonably may"; and the rule, it is said, "requires a repurchase of the stock in a reasonable time."[14] A recent New York case[15] shows to what confusion this rule, if blindly followed, would lead, and also how impossible it is to part company permanently with the fundamental measure of the value at the time of conversion. Brokers converted stock purchased for a customer, but after the conversion and without knowledge of it the latter advanced additional margin. It was held that the brokers were responsible for the value of the stock at the time of the conversion, although the stock *declined* later and the customer *would not have realized so much on the stock by replacing himself within a reasonable time after discovery of the conversion.* Treating the rule in *Baker* v. *Drake* as a rule of *duty to replace,* would have given the plaintiff about one-third of what he had paid out in cash, most of it after the conversion, and the defendants would have gained as profits the total amount of the decline in the stock. On this point the court said:[16]

"* * * I think that it may confidently be asserted that the Court of Appeals have never decided or suggested that one guilty of conversion could profit by the decline in the market value of the thing converted between the time of the conversion and the discovery of it by the party injured. *The general rule of damage, of course, is the value of the thing converted at the time and place of the conversion, together with interest thereon from the time of the conversion, and that rule should be adopted in the absence of special circumstances, whereby it will not afford complete indemnity to the injured party.*

"The early cases made a distinction in case the property con-

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[12]Burnham *v.* Lawson (N. Y. 1907) 118 App. Div. 389, 103 N. Y. Supp. 482.

[13]Hurt *v.* Miller (N. Y. 1907) 120 App. Div. 833, 105 N. Y. Supp. 775.

[14](1888) 110 N. Y. 237, 248.

[15]McIntyre *v.* Whitney (N. Y. 1910) 139 App. Div. 557, 124 N. Y. Supp. 234, affirmed (1911) 201 N. Y. 526.

[16](N. Y. 1910) 139 App. Div. 557, 558. Italics inserted.

verted was of fluctuating value, so as to give the party injured the benefit of a rising market. The distinction was not confined to speculative stock transactions, and I perceive no reason for treating such transactions as *sui generis.* It was finally decided in *Markham* v. *Jaudon* (41 N. Y. 235) in the case of a speculative stock transaction, that the customer was entitled to the highest market price of the property between the time of the conversion and the trial. That rule was limited in *Baker* v. *Drake,* in which it was held that, upon discovering the conversion, the customer could not lie by and mulct the defendant for a conjectural loss based upon the highest value which the stock might attain over an indefinite period thereafter, but that if he wished to continue the venture and to charge his broker for the loss of speculative profits, it was his duty within a reasonable time to replace the stock, thus averting further damage. Judge Rapallo discussed the earlier cases, and it is, therefore, unnecessary to extend this opinion by reference to them. From his discussion it is apparent that he was considering solely *the right* of the injured party to recover speculative profits in addition to what was realized by the broker from the unlawful sale. * * *"

Ingraham, *P. J.*, dissented on the ground that the action was "strictly for conversion," and that consequently plaintiff was limited to the damages sustained by him on the day of conversion. But this leaves out of view the possibility of consequential damages. The decision evidently depends upon replacement being a privilege and not a duty. Plaintiff is under no obligation to replace himself, in case of a decline, in order that the defendant may profit by his own wrong,[17] but he may recover the consequential, in addition to the direct damages.

The latest case in the New York Court of Appeals contains a dictum developing a startling extension of the idea of the so-called *duty* of replacement. In Weld *v.* Postal Telegraph Cable Co.[18] the action was for negligence in the transmission of a message sent in December, directing plaintiff's agent to sell cotton deliverable in March, *March cotton,* at 12.70. As received, the message read "12.07." This error was acted on and the cotton sold at a loss. The case went off on another point, but the court, on the subject of the avoidance of consequences, through replacement in the market, says that it was not only "the duty of the plaintiffs to exercise reasonable diligence to minimize their damages," but that "it was equally their duty to annihilate them if they could." We have here a distinctly novel conception which completes the transformation of the doctrine of avoidable consequences. Instead of

[17] Taussig *v.* Hart (1874) 58 N. Y. 425.

[18] (1910) 199 N. Y. 88. 92 N. E. 415.

its being founded on the idea that consequences, which plaintiff in the natural and normal effort to save himself from loss, can avoid, are *remote,* it is that the plaintiff is under a duty to the defendant to reduce his own damages; that the measure of this duty is reasonable care. In this view it would seem to be inevitable that in every action, the normal measure of damages having been ascertained, the next question would be: Has the plaintiff used due care to reduce them, as far as possible, by replacing himself by means of making a contract with a third person—a duty which, as we have attempted to show, does not exist.

As already explained, the duty, if it exists at all, must exist in all classes of cases, whether sounding in tort or contract or both. It seems to be a necessary consequence that *plaintiff* should prove that he has discharged it, before he can recover. But on the contrary, the rule is that defendant must always show that the plaintiff lost a reasonable opportunity to replace himself, that is, unreasonably enhanced the damages, or failed to reduce them. The English courts have examined the matter carefully in cases of contracts for the purchase and sale of chattels, and have held practically that there is no such thing as a general duty resting upon the plaintiff to make a "forward contract." The following extract from the opinion of Kelly, C. B., in *Brown* v. *Muller*[19] puts the matter in its true light, and has been generally followed as sound law:

"It has been argued with much ingenuity that the damages ought to be estimated at a lower figure if it appear that when the defendant announced his intention of not delivering, or at all events when the first breach took place, and it became apparent that the contract could never be performed at all, the plaintiff might have entered into a new contract to the same effect as the old one for the months of October and November on as favorable terms; and if the plaintiff, on hearing he would never get delivery, was bound to go and obtain, if he could, the new contract suggested, then, no doubt, assuming that he might have made such a contract, the damages ought to be limited to his loss at that time. But there was, in my opinion, no such obligation. He is not bound to enter into such a contract, which might be either to his advantage or detriment, according as the market might fall or rise. If it fell, the defendant might fairly say that the plaintiff had no right to enter into a speculative contract, and insist that he was not called upon to pay a greater difference than would have existed had the plaintiff held his hand. Or again, by such a course, the plaintiff might be seriously injured and yet have no remedy. Suppose, for example, his new contract was with a person who proved insolvent.

[19](1872) L. R. 7 Ex. 319, 322 (a breach of contract to deliver goods).

He would, in that case, be without redress; he would have lost his former contract, and his new one would turn out worthless. In either event, therefore, I do not think the plaintiff could be called upon to enter into a fresh contract. If he did, and thus obtained an advantage, he no doubt might save the defendant from some damages. But if he should suffer a loss, as by the insolvency of the new contractor, he could not make the defendant answer for it. And if it should happen that he might have done better for the defendant by waiting and making no speculative contract, the defendant would in his turn have a fair right to complain that his loss had not been mitigated as far as possible."[20]

It may be well, in conclusion, to refer to a case which is sometimes erroneously thought to support the idea of a duty to replace. *Startup* v. *Cortazzi*[21] was *assumpsit* for non-delivery of linseed pursuant to a contract of sale. Plaintiffs contended that as they had paid a portion of the purchase money in advance they were entitled to damages according to the price at the time of trial. But the rule sustained was the price at the time fixed for delivery. There was no proof of any special damages or loss of speculative profits, nor that the plaintiffs had not the means of replacing themselves, but it seems to have been thought by the judges that had there been circumstances of this sort, the fact that the plaintiffs had parted with the money in advance would have enabled them to have the benefit of the higher rule of damages.

The case therefore is merely one of those which shows that consequential damages may in the case of sales be recovered, and that the plaintiff is not always confined to value at the time and place of delivery. It shows that there is a connection between claiming the profits of a speculation and replacement, which is a sound idea. But there is nothing to show that the plaintiff is under a duty to replace himself in the market.

Replacement not being a duty, proof of it cannot be a part of the plaintiff's case; the proof that plaintiff might have replaced himself, or did replace himself, must come, if not admitted by him, from the defendant. In all such cases, it is an application of the rule of avoidable consequences.[22]

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[20] *Cf.* Roper *v.* Johnson (1873) L. R. 8 C. P. 167; Michael *v.* Hart [1902] 1 K. B. 482; Burnham *v.* Lawson (1902) 103 N. Y. Supp. 482, 118 App. Div. 389; Hurt *v.* Miller (1902) 105 N. Y. Supp. 775, 120 App. Div. 833.

[21] (1835) 2 C. M. & R. 165.

[22] From advance sheets of Sedgwick on Damages, Ninth Edition.